

## MCLE ON THE WEB (\$15 PER CREDIT HOUR)

### TEST #5

### 1 HOUR CREDIT

### LEGAL ETHICS (Part 2)

To earn 1 hour of MCLE credit in the special category Legal Ethics, read the substantive material, then download the test, answer the questions and follow the directions to submit for credit.

## **Attorney Client Deals**

Walking through the basic steps of compliance and documentation within rule 3-300

By Ellen Peck

In the previous test, I discussed types of attorney/client deals which require compliance with Rule of Professional Conduct 3-300 and those that don't.

In part two, we will assume that the lawyer/client deal is within the ambit of rule 3-300 and walk through the basic steps of compliance and documentation.

### **The basic steps**

Basic compliance with rule 3-300 requires that each of the following components be met:

1. The transaction or acquisition and its terms are fair and reasonable to the client. (Rule 3-300(A))
2. The transaction or acquisition and its terms must be transmitted in writing to the client in a manner which should reasonably have been understood by the client. (Rule 3-300(A))
3. The client must be advised in writing that the client may seek the advice of an independent lawyer of the client's choice. (Rule 3-300(B))
4. The client must be given a reasonable opportunity to seek that advice. (Rule 3-300(B))
5. After the occurrence of all of the foregoing, the client must consent in writing to the terms of the transaction or acquisition. (Rule 3-300(C))

### **Compliance steps**

The following steps are suggested in order to comply with these requirements. They are the suggestions of the author only and do not necessarily set forth the standard of care or ensure compliance with rule 3-300 in every case.

### **STEP ONE:**

#### ***Document the terms of the transaction in writing.***

Once you and the client have agreed upon the terms of the business transaction or acquisition, prepare the requisite writing describing the terms and conditions of the deal with the client. At this point, the lawyer should determine whether the deal is fair and reasonable to the client and in terms which can be reasonably understood by the individual client.

If an independent counsel assists the client, that independent counsel will also have the duty of explaining the language and terms of the agreement as well as assisting the client to determine whether the terms are fair and reasonable. However, you should not rely upon independent counsel to fulfill that responsibility. If the client declines the assistance of

independent counsel, you or your firm should go over the terms in the document for fairness, reasonableness and comprehensibility of that specific client.

Each transaction is different and each client is different, calling for varying degrees of scrutiny.

### **General questions**

However, here are some of the general questions to think about, although the failure to do any of them may not fall beneath the standard of care:

1. Analyze the terms and conditions as if you were the independent counsel for the client and you were your own adversary.

- \* Are there terms and conditions which are unfair?

- \* Has the value of the property to become the security been agreed to by the client or established by an independent third party?

- \* Should you ask another lawyer in the firm or a friend to look at it from a fairness perspective?

- \* Are other terms, conditions or information needed to establish that the transaction or acquisition is fair and reasonable?

2. Are the terms of the transaction or acquisition in language that the client can understand?

- \* If English is not the first language of the client, you might have all of the documents translated into the client's first language.

- \* Do you need to explain other terms or language to make the writing comprehensible?

- \* Do you have to explain the consequences of the transaction or acquisition in order to understand the terms and conditions of the written deal?

### **Transmission**

Once you have prepared a writing which describes the terms and conditions of the transaction and you have satisfied yourself that a judge, arbitrator or jury might find the transaction reasonable and fair to the client, transmit the writing to the client.

### ***STEP TWO:***

***Give a written advisement of the opportunity to seek independent counsel of the client's choice.***

On the first occasion (usually the initial consultation or interview) in which a security interest is discussed with a prospective client, you should orally discuss with the client that they should consult an independent lawyer on giving a security interest. It is suggested that you follow this procedure when you transmit the written terms and conditions:

1. Some form which has a written advisement of the client's opportunity to seek the advice of independent counsel of the client's choice must be given at the time that the documents regarding the transaction are given to the client. (Rule 3-300(B))

2. A responsible attorney must document the following:

- \* The date of delivery of the written advisement to the client;

- \* The name of the responsible attorney who delivered the written advisement; and

- \* The written acknowledgement of the client that the client received and read the written advisement.

3. No fee agreement or other documentation should be signed by the client until the remainder of the process set forth below is completed.

### **Security interest**

The fee agreement is the ideal place for a security interest to be set forth if it is the commencement of representation. If a security is acquired after commencement, you will probably want to create a separate writing to keep intact your original fee agreement. If a lawyer is acquiring a security interest for past due fees, the lawyer should follow this same process.

Any office that enters into a security agreement with a client should have a written advisement form for this purpose. This form can be generated anew, photocopied or be on a preprinted NCR form. However, it is absolutely essential that the attorney deliver a copy of the writing (advising the client to seek the advice of independent counsel) to the client in every case and keep at least one copy for the files for later proof in case of State Bar inquiry, legal malpractice claim, fee dispute or collection proceeding.

### **Frequent violation**

The failure to give a written advisement is the most frequently violated portion of the rule. Neither the Supreme Court nor the State Bar Court recognize "substantial" compliance with the rule.

Failure to advise the client to seek the advice of independent counsel alone establishes a violation of rule 3-300 and is cause for discipline. (See *Ritter v. State Bar* (1985) 40 Cal.3d 595, 606, 221 Cal.Rptr. 134; *Arden v. State Bar* (1987) 43 Cal.3d 713, 725-726, 239 Cal.Rptr. 68.)

Failure to comply with the written requirement to advise the client that he has an opportunity to seek independent counsel is not deemed to be a "technical" violation of the rule by the California Supreme Court. (*Brockway v. State Bar* (1991) 53 Cal.3d 51, 278 Cal.Rptr. 489.)

A lawyer or law firm acquiring a lien should never recommend any lawyer to any client for this purpose.

A member, associate or partner of the law firm is not "independent" counsel within the meaning of the rule. (*Connor v. State Bar* (1990) 50 Cal.3d 1047, 269 Cal.Rptr. 742.)

"Independent counsel" is probably not the following: any lawyer who serves "of counsel" to you or your firm, any lawyers who share space with the lawyer acquiring a security interest, or any lawyer or law firm with which the firm acquiring the interest has any regular relationship.

Obviously, any recommendation of another lawyer by you or your firm will cast doubt upon the recommended lawyer's independence.

### **STEP THREE:**

***The client must be given an opportunity to seek the advice of independent counsel.***

Rule 3-300(B) also requires that the client be given a reasonable opportunity to seek the advice of an independent lawyer of the client's choice.

### **What is reasonable?**

Neither the rule nor case law specifies what constitutes a "reasonable opportunity."

However, there should be some period of time between the written advisement to obtain independent counsel and the signature of the client to any lawyer/client transaction or fee agreement by which you or your firm acquires a security interest.

1. The client who declines to consult an independent attorney.

Not all clients will want to go to an independent lawyer before entering into a security interest and you cannot force the client to consult such an attorney against his or her will.

You or your firm should decide to adopt a general policy concerning acceptance of a security interest if the client does not wish to retain independent counsel.

This decision is a business decision. If you or your firm decide to go forward with the transaction or accept a security interest after a client declines to seek independent counsel, it behooves you to document carefully that the client has truly had some period of time to reflect on whether to retain independent counsel.

### **A three-day rule**

I tend to favor a three-day rule of thumb because there are a number of statutes in California that allow an individual three days to withdraw from a contract.

If you decide to enter into the security interest, give the client at least a three-day cooling off period between the written advisement and a client's execution of the fee agreement or other document with a security interest provision in circumstances where the client declines to consult an independent attorney.

Unless earlier retention is essential to protect the client's interest, the cooling off period should be followed in all cases.

In order to get a description of the property which is being used as security, you will often need to acquire documentation from the client.

This will delay your preparation of the security agreement, promissory note and other documentation.

You will have less risk from charges of overreaching if you give the client some time to review the documents creating the lien before entering into it.

### **Document the date**

A good rule of thumb is to give the client the proposed documents at least one full day (preferably three days) prior to signing any papers or fee agreement through which the attorney requires a security for fees. Document, in writing, the date upon which you deliver the proposed papers to the client.

If urgency situations call for deviation from this standard, the urgency should be carefully documented in writing and the client should sign or initial the provision which states that the client desires to go forward without further delay.

### **2. The client who consults an independent attorney.**

If the prospective client consults an independent attorney, you or your law firm should:

- \* Prepare all written documentation for the security interest and/or fee agreement (in compliance with the writing requirement of rule 3-300(A));
- \* Document the transmission of proposed documents, including the proposed fee agreement, to the independent attorney (in compliance with the transmission requirement of rule 3-300(A));
- \* Verify with the independent attorney that the consultation took place and determine, if possible, the date of the consultation; and
- \* Memorialize in writing your verification process.

After the foregoing process has taken place, the fee agreement with a security interest may be executed at any time that the client, in consultation with independent counsel, feels comfortable with it, preferably before any legal services are rendered.

### **Emergency situation**

Since Business & Professions Code §6148(d)(1) permits an attorney to render services in an emergency to avoid foreseeable prejudice to the rights or interests of the client without a written agreement, in such circumstances you can begin work in an urgency situation.

3. Your fee agreement, lien documents of other writing concerning the lawyer/client deal should memorialize the process.

### **Sample provisions**

The following sample provisions (or similar provisions) can be added to your fee agreement or used in documenting the creation of a lien or other security.

"Client further represents, warrants and acknowledges that on (date), (name of attorney or other personnel) advised Client in writing that Client had an opportunity to seek the advice of independent counsel to review this (fee agreement, retainer letter) as well as the (documents creating the security interest, e.g., 'Note, and the Deed of Trust, and the related documents')."

### **Checking alternatives**

The attorney responsible for creating the form should be responsible for checking one of the following alternatives:

a. "Client advised (name of attorney or firm) on (date) that Client has had an opportunity to seek the advice of independent counsel but declined to do so. On (date), prior to executing this retainer, Client received a complete copy of the proposed (documents creating lien, e.g. fee agreement or retainer letter, the proposed note, proposed deed of trust and other proposed documents relating to this transaction)."

b. "Client advised (name of attorney or firm) that your counsel for this purpose is (name of independent counsel and address). At Client's direction, (name of attorney or firm) delivered the proposed (documents creating lien, e.g. fee agreement or retainer letter, the proposed note, proposed deed of trust and other proposed documents relating to this transaction) to (name of independent counsel) for review on (date)."

### **Further safeguard**

A further safeguard is to have the client initial the foregoing paragraphs on the document to demonstrate that the client has read those provisions.

### **STEP FOUR:**

#### ***Obtain the client's written consent.***

Rule 3-300(C) requires that the client consent in writing to the terms of the transaction or acquisition. Once again, oral consent to a security interest (e.g. the "pink slip" to a vehicle or a mink coat being held by the lawyer) creates a violation of the rule for which discipline can be imposed or which can interfere with the lawyer's ability to collect a fee.

From a risk management standpoint, I encourage you to have every security interest transaction reviewed by another attorney in your firm (who is specially appointed to review such matters) or by another lawyer whom you trust, if you are a sole practitioner.

### **Attorney review**

Another lawyer may point out a provision that you forgot or a section that might be challenged as ambiguous by another lawyer.

Because rule 3-300 challenges are so frequent and have such serious consequences, this "audit" procedure should occur before the final fee agreement is executed.

While these procedures may take a little time to implement up front, they can be automated within your practice to take very little time after implementation.

With the proper procedures and forms in place, you can turn your full energies to representing your clients rather than worrying about your own risk.

*Ellen R. Peck, a former trial judge of the State Bar Court, practices law in Malibu. She is a co-author of the Rutter Group's California Practice Guide — Professional Responsibility and serves as a neutral mediator and arbitrator on the Lawyers' Practice Panel of the American Arbitration Association.*

## **Test — Legal Ethics**

### **1 Hour MCLE Credit**

This test will earn 1 hour of MCLE credit in Legal Ethics.

1. True/False. Rule 3-300 requires that any transaction with a client also be fair to the lawyer.
2. True/False. Compliance with rule 3-300 requires that the written terms of the transaction must be read by the client in the lawyer's presence.
3. True/False. The written terms must be in language which can be reasonably understood by the client.
4. True/False. The client must be advised in writing that he/she may seek independent legal advice.
5. True/False. The sophisticated client can waive the requirement that he/she consent in writing to the terms of the transaction.
6. True/False. If the client has trouble finding independent counsel, you should recommend someone.
7. True/False. If the client does not wish to have independent counsel, refuse to sign the agreement.
8. True/False. If the client does not wish to have independent counsel, you must have another lawyer in your firm act as his lawyer.
9. True/False. A security agreement should not be in the fee agreement.
10. True/False. Failure to give written advisement of a security agreement is the most frequent violation of this rule.
11. True/False. Rule 3-300 is very specific as to what constitutes a reasonable time period for the client to seek independent legal advice.
12. True/False. The three day rule of thumb regarding a reasonable time period within which the client has an opportunity to consult independent counsel is just the wishful thinking of this author.
13. True/False. If an urgent situation demands deviation from your firm's arbitrary definition of "reasonable opportunity to consult with independent counsel," document the deviation.

14. True/False. The requirement that a client must consult in writing to a security interest means that you and the client just have to execute the requisite "pink slip" of a vehicle which is intended to secure the attorney's fees.
15. True/False. The client must consent in writing to the terms of the transaction only if he/she does not get independent legal counsel.
16. True/False. If the client gets independent counsel, you do not have a duty to explain the terms of the agreement to the client.
17. True/False. If English is not the first language of the client, you must translate the terms of the agreement into the client's language.
18. True/False. Substantial compliance with rule 3-300 will keep you out of trouble if you are prosecuted.
19. True/False. If a client does not get independent counsel, you should have him/her sign a statement to that effect.
20. True/False. Compliance with rule 3-300 is so easy that you almost never need to use colleagues as a sounding board or consultant.

### **Certification**

- This activity has been approved for Minimum Continuing Legal Education credit by the State Bar of California in the amount of 1 hour, of which one hour will apply to legal ethics.
- The State Bar of California certifies that this activity conforms to the standards for approved education activities prescribed by the rules and regulations of the State Bar of California governing minimum continuing legal education.

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- Print the **answer form only** and answer the test questions.
- Mail **only form and check** for \$15 to:

**MCLE on the Web**

**The State Bar of California**

**Attn: Ibrahim Bah**

**180 Howard Street**

**San Francisco, CA 94105**

- Make checks payable to State Bar of California.
- A CLE certificate will be mailed to you within eight weeks.

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Name

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Law Firm/Organization

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Address

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State/Zip

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State Bar Number (Required)

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|--------------------------|--------------------------|
| 1. TRUE ____ FALSE ____  | 11. TRUE ____ FALSE ____ |
| 2. TRUE ____ FALSE ____  | 12. TRUE ____ FALSE ____ |
| 3. TRUE ____ FALSE ____  | 13. TRUE ____ FALSE ____ |
| 4. TRUE ____ FALSE ____  | 14. TRUE ____ FALSE ____ |
| 5. TRUE ____ FALSE ____  | 15. TRUE ____ FALSE ____ |
| 6. TRUE ____ FALSE ____  | 16. TRUE ____ FALSE ____ |
| 7. TRUE ____ FALSE ____  | 17. TRUE ____ FALSE ____ |
| 8. TRUE ____ FALSE ____  | 18. TRUE ____ FALSE ____ |
| 9. TRUE ____ FALSE ____  | 19. TRUE ____ FALSE ____ |
| 10. TRUE ____ FALSE ____ | 20. TRUE ____ FALSE ____ |